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SUBJECT: Over-Capacity Not a Concern in Zhanjiang and Beihai

REF: A) BEIJING 3349, B) GUANGZHOU 643

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¶1. (SBU) Summary: Big plans for industrial expansion are underway in Beihai and Zhanjiang near the southern end of China's coast, where local officials recently described to the Consul General ambitious plans to develop steel, petrochemical, ship building, export processing and other manufacturing industries. Beihai (population 1.5 million) is building the Tieshan Port Industrial Zone with plans for new deep water port facilities with 200 berths and 132 square kilometers allotted to five industries. The zone is one of eight new industrial parks that are part of the central government's Beibu Gulf Economic Development Zone in southern Guangxi Zhuang Autonomous region; ASEAN trade is a major focus. Neighboring Zhanjiang (population 7+ million) in Guangdong Province is the site for a planned 10 million ton per year steel mill and a Sinopec-Kuwait joint-venture petrochemical facility that will have the capacity to refine 15 million tons of oil. Despite recent concerns expressed by business leaders, academics and officials elsewhere in China about the threat of over-capacity in some of these same industries (ref A), the mood in these third-tier cities seems to be full steam ahead. Interlocutors expressed interest in U.S. participation in trade and investment opportunities in steel mill and petro-chemical systems and controls, port handling equipment and management, and wastewater treatment, as well as clean energy and environmental protection equipment. End summary.

Beihai Building a New Industrial Zone

¶2. (SBU) Beihai on Guangxi's Gulf of Tonkin coast is the site of a major new industrial zone that's part of Guangxi's larger Beibu Gulf Development Zone. When the CG visited the embryonic Tieshan Port Industrial Zone on December 8 it consisted of little more than several dozen square kilometers of bulldozed land, the beginnings of

some roads and a single operational pier. However, local officials have ambitious plans. The government has set aside 400 square kilometers for the zone, where it is developing a deep water port with depths ranging from 10-22 meters. Beihai Vice Mayor Yang Zhiyuan claimed that it was the only deep water port in China that still has space for large-scale industrial development. Officials plan to eventually build more than 200 berths that can accommodate vessels ranging from 10,000 to 200,000 tons. The industrial zone initially has 132 square kilometers allotted to five industries -- petrochemicals, logistics, pulp and paper products, ship building, and export processing.

Major Projects: Oil Refinery and Paper Pulp Plant

13. (SBU) According to Feng Wei, the Deputy Director of the Construction and Administrative Committee Office of the Beihai Beibu Gulf Economic Zone, the centerpiece of the petrochemical zone will be a Sinopec oil refinery with the capacity to produce eight million tons of gasoline and 200,000 tons of polyphenyl ether (PPE) per year. In addition, officials also plan for a liquefied natural gas (LNG) wharf and storage facilities. (NOTE: Press reports mention discussions with British Petroleum as a partner.) A joint-venture including Finnish paper manufacturer Stora Enso is the main investor in the building

14. (SBU) Feng explained that the logistics zone would be designed

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for a capacity of more than 300 million tons of bulk and container cargo. The export processing zone will comprise 10 square kilometers with room for 1,000 labor-intensive export makers, he said. The firms will be required to build facilities of at least four stories to save space. Ship building was the only sector where officials expressed caution about development plans because of current surplus capacity in China.

Focus on and Preparing for ASEAN Trade

15. (SBU) The Tieshan zone is just one of eight new industrial parks planned in the Beibu Gulf Development Zone, which includes four municipalities in the Guangxi Zhuang Autonomous Region, namely Beihai, Fanchenggang, Nanning and Qinzhou. The Guangxi government plans to spend RMB one billion annually in support of the development of the zones, according to Vice Mayor Yang. But Feng noted that the Beihai local government and private investors will fund most of the development costs. Mayor Lian Younong pointed out to the CG that the State Council wants the area to serve as a platform for China-ASEAN regional cooperation. However Vice Mayor Yang commented that cooperation with ASEAN is still in its early stages and investment from ASEAN countries in Beihai is still small.

Zhanjiang Pursues Major Steel and Chemical Plants

16. (SBU) Zhanjiang, the coastal Guangdong city across the peninsula and provincial border from Beihai, also has big plans for industrial development. Mayor Ruan Risheng explained to the CG that the capacity of the planned Baosteel steel mill will be 10 million tons per year. The Sinopec-Kuwait joint-venture petrochemical plant, which was transferred to Zhanjiang from Nansha District in Guangzhou due to environmental concerns of local residents, will have the capacity to refine 15 million tons of oil and one million tons of ethylene annually, according to Ruan. Zhong Hongli, the Deputy Chief Engineer of Sinopec Zhanjiang Dongxing Petrochemical Co., told the CG that the new refinery plan is still pending a local environmental assessment.

17. (SBU) The Baosteel and Sinopec-Kuwait projects will be located on Donghai Island, where new port facilities are also being constructed. According to Zhanjiang Port Deputy Party Secretary Yang Wen, construction is scheduled to last 30 years and the new port will occupy five square kilometers. The port plans to build

one new 300,000-ton class oil terminal next year and another 300,000-ton class bulk cargo terminal shortly thereafter. The port expects to increase annual throughput capacity by 100 million tons over the next three to five years, according to Deputy Party Secretary Yang.

¶8. (SBU) Yang also noted that the port and Zhanjiang's industrial development in general will benefit from stimulus spending on the construction of railways that currently transport about 70% of bulk cargo to and from the port. He said that port officials have detected signals from the recent Central Economic Work Conference that have encouraged them to speed their investment in port expansion.

Comment - Few Concerns of Overcapacity

¶9. (SBU) Comment: Massive industrial development plans in Beihai and Zhanjiang suggest that overcapacity is of little concern in China's third-tier cities. The two major development zones that Congenoffs discussed with local officials focus on three of the six industries highlighted in the recent European Union Chamber of Commerce report on over-capacity -- steel, chemicals and refining (ref A). Beihai officials acknowledge that they may need to be cautious about moving forward with development of the ship-building

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industry because of over-capacity, but, with an estimated 10 percent of the global shipping fleet already idle (ref B), this may be an understatement. Beihai is also forging ahead with its plans for major expansion of the export processing industry despite the global economic downturn's negative effects on China's markets overseas. Academics, businessmen and officials in China's first-tier cities may worry about the threat of industrial over-capacity, but it appears those concerns have yet to filter down to places like Zhanjiang and Beihai. End Comment.

¶10. (SBU) The CG's December 7-10 trip to Beihai and Zhanjiang also included meetings with the Beihai Civil Volunteers Association (septel), Guangxi COFCO Bio-Energy Company (septel), the Beihai China Council for the Promotion of International Trade (CCPIT) and members of the local business community, Beihai College of the Beijing University of Aeronautics and Astronautics, Guangdong Ocean University, the Zhanjiang CCPIT and business leaders, Guolian Aquatic Products Company, and Cyclare Technologies Inc. In addition, the CG spoke to students at Beihai College, met with the press in Beihai and donated books to the Zhanjiang Municipal Library.

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